IN THE
SUPREME COURT OF MISSOURI

No. SC85781

MEDICINE SHOPPE INTERNATIONAL, INC.,

Respondent,

v.

DIRECTOR OF REVENUE,

Appellant.

APPELLANT'S BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutory and Constitutional Authorities

Other Authorities

JURISDICTIONAL STATEMENT

This case came before the Administrative Hearing Commission on complaints filed by Medicine Shoppe International, Inc. Medicine Shoppe challenged the Director of Revenue's assessment of income tax and interest. On December 23, 2003, the Commission ruled in favor of Medicine Shoppe.

Because the questions posed in this appeal involve the construction of the revenue laws of the state (MO. CONST. art. V, § 3), and because by statute petitions for review of Commission decisions are brought to this Court when the issues fall within its jurisdiction (§ 621.189, RSMo.), jurisdiction is proper in this Court.

STATEMENT OF FACTS

This case arises from the Director's assessment of additional taxes for the years 1998, 1999, and 2000.

Medicine Shoppe International, Inc., as this court observed in *Medicine Shoppe International v. Director of Revenue*, 75 S.W. 3d 731, 732 (Mo. banc 2002), is in the business of "franchising retail pharmacies." Medicine Shoppe's headquarters are in Missouri. Appendix A3. Medicine Shoppe had no offices outside Missouri, "[a]ll its officers were located in Missouri, and all but a couple of its approximately 200 employees were located in Missouri." A4.

In the years at issue, Medicine Shoppe was a subsidiary of Cardinal Health, whose corporate headquarters were in Ohio. *Id*.

Prior to the periods at issue, Medicine Shoppe entered into an agreement with Cardinal, under which any Medicine Shoppe funds were swept each business day into a Cardinal account. A 4-6. Cardinal then both paid "investment returns" back to Medicine Shoppe, and returned to Medicine Shoppe whatever funds it needed to operate its business. A5-7. "[A]ll notices and communications under the agreement [are] made to Medicine Shoppe at its St. Louis, Missouri, address." A6. But "Medicine Shoppe has no control over where the funds are invested."

For the tax years in question, Medicine Shoppe earned considerable sums on its investments: $5,351,747 in 1998; $5,697,550 in 1999; and $6,809,956 in 2000. A8. For each year, Medicine Shoppe elected to use single-factor apportionment. A9. Medicine Shoppe classified the investment income it received from Cardinal as "non-Missouri source income," and excluded it from single-factor apportionment on its Missouri corporate income tax returns. A10-A15.

The Director issued Medicine Shoppe notices of adjustment, removing the investment income from the "non-Missouri source" category, and thus inserting it back into the single-factor apportionment formula. A15-A17. Medicine Shoppe protested the assessments in letters dated October 15, 2001 (tax year 1999) and September 18, 2002 (1998 and 2000). A15, A17. On June 5, 2002, the Director issued a final decision disallowing Medicine Shoppe's treatment of the 1999 investment income as non-Missouri source income. A16. On December 18, 2002, the Director issued similar decisions as to 1998 and 2000. A17.

Medicine Shoppe filed complaints with the Administrative Hearing Commission on July 2, 2002, as to the decision for 1999, and on January 14, 2003, as to the decisions for 1998 and 2000. A1-

A2. On December 23, 2003, the Commission ruled in favor of Medicine Shoppe. According to the Commission, "Medicine Shoppe was entitled to allocate its investment interest income from Cardinal Health prior to application of the Missouri single-factor apportionment fraction." A38. In other words, the fraction was properly applied, according to the Commission, not to Medicine Shoppe's total income, but only to its income derived from Missouri.

The Director filed a timely petition for review.

POINT RELIED ON

The Administrative Hearing Commission erred in excluding in its entirety investment income from the calculation of tax because the taxpayer, having chosen single-factor apportionment under § 143.451.2(2), RSMo., was required to include investment income, even from out-of-state sources, in the multiplicand in that such income is part of the taxpayer's "net income" or its "total income from all sources."

Acme Royalty Co. v. Director of Revenue, 96 S.W.3d 72 (Mo. banc 2002)

§ 143.451, RSMo. 2000

§ 143.461, RSMo. 2000

ARGUMENT

The Administrative Hearing Commission erred in excluding in its entirety investment income from the calculation of tax because the taxpayer, having chosen single-factor apportionment under § 143.451.2(2), was required to include investment income, even from out-of-state sources, in the multiplicand in that such income is part of the taxpayer's "net income" or its "total income from all sources."

Standard of Review

This is an appeal from a decision by the Missouri Administrative Hearing Commission. The Commission's decisions are upheld when authorized by law and supported by competent and substantial evidence upon the record as a whole, and when they are not clearly contrary to the reasonable expectations of the General Assembly. *See Becker Elec. Co. v. Director of Revenue*, 749 S.W.2d 403, 405 (Mo. banc 1988); § 621.193, RSMo. 2000. This Court, in essence, adopts the Commission's factual findings. *See Concord Publ'g House v. Director of Revenue*, 916 S.W.2d 186, 189 (Mo. banc 1996).

The Commission's decisions on questions of law are matters for this Court's independent judgment. *La-Z-Boy Chair Co. v. Director of Economic Development*, 983 S.W.2d 523, 524-25 (Mo. banc 1999); *Hewitt Well Drilling & Pump Service, Inc. v. Director of Revenue*, 847 S.W.2d 797, 797 (Mo. banc 1993).

Respondent Medicine Shoppe, Inc, had the burden of proof before the Commission. *See* § 621.050.2, RSMo 2000.

Introduction

As she did in *Medicine Shoppe International, Inc. v. Director of Revenue*, 75 S.W.3d 731 (Mo. banc 2002) (*Medicine Shoppe I*), the Director here asks the Court to return to the basic, statutory rules by which corporations determine their Missouri taxable income. Those rules require that corporations pay tax on all income derived from Missouri. Rather than require a corporation to determine the source of each dollar, however, the statutes permit the use of formulas to substitute for precise (and often impractical) accounting. Use of those formulas may result in a higher or a lower tax than would precise accounting. But they are used solely at the taxpayer's option. Hence, their use is likely only when they result in lower expense – taxes paid plus the expense of calculating and defending the calculations – than would specific, dollar-by-dollar accounting.

Here, Medicine Shoppe chose to use one of those formulas: "single factor apportionment," permitted under § 143.451. Single factor apportionment does not exempt any income from taxation. It is, rather, a substitute means of determining what portion of a corporation's net income from all sources is assumed to have been

derived from Missouri. Unfortunately, bound by this Court's precedents, the Administrative Hearing Commission here held single factor apportionment renders some of Medicine Shoppe's income untaxable – "nowhere income," to use the Commission's words. App. A29. But this Court should enforce the statute as it was written, thus eliminating the prospect of "nowhere income" and refusing to give corporations a bounty for making bank deposits and similar capital investments outside, rather than inside the State.

I. Corporations are required to pay tax on all income derived from Missouri – which, after *Acme Royalty,* should not exclude income merely because the intangible that generated it was used outside Missouri.

Missouri imposes an income tax on corporations "in an amount equal to five percent of Missouri taxable income." § 143.071, RSMo. 2000. Medicine Shoppe has "Missouri taxable income." So it is subject to tax. The question here is what portion of Medicine Shoppe's total income is "Missouri taxable income."

"Missouri taxable income," for purposes of the corporate income tax, is "so much of" the corporation's "federal taxable income . . . as is derived from sources within Missouri as provided in section 143.451." § 143.431. The cross referenced section, § 143.451.1, begins by stating – without exception – the rule:

"Missouri taxable income shall include all income derived from sources within this state." § 143.451.1. Subsection 2 then reiterates that rule: "A corporation . . . shall include in its Missouri taxable income all income from sources within this state" – again, without any exceptions. § 143.451.2. Subsection 2 then explains that taxpayers cannot avoid the tax merely because some portion of their income is derived from transactions that involve multiple states: taxable income "includ[es] that from the transaction of business in this state and that from the transaction of business partly done in this state and partly done in another state or states." *Id*.

Before addressing the statutes that establish apportionment formulas, we address the meaning of "derived from sources within this state." Among the problematic issues in this regard is the treatment of investment income – income that is derived with little actual effort, from investment vehicles that could easily be purchased on either side of the state line. Particularly pertinent here are three decisions – the most recent of which is inconsistent with the rule in the other two.

In *Petition of Union Electric Co. of Missouri*, 161 S.W. 2d 969 (Mo. banc 1942), the Court addressed dividend and interest payments made to a Missouri corporation by companies located outside the

state. There, as under the current Missouri tax law, the ultimate issue was whether such interest and dividends constituted income from "sources in Missouri." The Court set out three categories of sources of "income": "(A) labor; (B) the use of capital . . .; and (C) profits derived from the sale or exchange of capital assets." *Id*. At 970. The Court then set out what would generally be the "source" of each category of income:

> It is said that the locus of the source of income is determined as follows: In the case of income derived from labor, it is the place where the labor is performed; in the case of income derived from the use of capital, it is the place where the capital is employed; and in the case of profits from the sale or exchange of capital assets, it is the place where the sale occurs.

Id. citing *In re Kansas City Star Co.*, 142 S.W. 2d 1029 (Mo. banc 1940). Addressing the taxation of dividends and interest payments to Union Electric, the Court thus looked to where the "actual use of capital" occurred, not to where the stock certificates or bonds might be held or where the dividends or interest might be payable. 161 S.W. 2d at 970-92. *See also Union Electric Co. v. Coale*, 146 S.W.2d 631 (Mo. 1940). As of 1942, then, income from interest paid on accounts placed

outside a State was income in the state where the funds were used, not in the state from which they were invested.

In *Medicine Shoppe I*, the taxpayer tried to invoke the *Union Electric* cases in its attempt to defined certain kinds of interest as non-Missouri-source income. This Court agreed that "categorizing or subdividing a corporation's revenue was rejected in" *Bank Building and Equipment Corp. of America v. Director of Revenue*, 687 S.W. 2d 168, 171 (Mo. banc 1989). But it noted that "[t]he *Union Electric* cases retain vitality to the extent that they recognize that wholly passive investments outside the state of Missouri are not included in the taxation formula used to determined Missouri taxable income," 75 S.W.3d at 735, *i.e.*, that "investments" do not become Missouri-source income unless they involve some effort on the part of the taxpayer within Missouri. In other words, the rule was that when capital is used in a state other than Missouri, the income derived from it is taxable there, not here.

That is inconsistent with the more recent holding in *Acme Royalty Co. v. Director of Revenue*, 96 S.W.3d 72 (Mo. banc 2002). The income at issue there, too, was investment income – *i.e.*, income from intangible property, indistinguishable in this sense from the "capital" addressed in *Union Electric* and *Medicine Shoppe I* – that was owned by a taxpayer in one state (there, Deleware) but used in another (Missouri). The

Court held that for such investment income to be taxable in Missouri, it was no longer enough that the asset was used in Missouri. *Id*. at 75. Rather, there had to be "some activity by the *taxpayer* in Missouri. *Id*.

The necessary result of *Acme Royalty* is to change the rule that has existed since *Union Electric*, under which if capital or another intangible asset is used exclusively in one place, income paid on that use is derived from that place, and not from the place from which the intangible was sent. Under *Acme Royalty*, were Company X, located in Illinois, to send to Missouri capital or another intangible, the income from the use of that capital or intangible in Missouri would not be taxable in Missouri unless that company itself undertook some activity in Missouri. The only way to reconcile that rule with the one in *Union Electric* is to conclude that the Commission is right, and that there is a category of "nowhere income" – a result that cannot be reconciled with the intent manifest in any provision of Missouri corporate income tax law.

That a corporation buys a certificate of deposit, for example, from a Missouri or an Illinois bank should not be dispositive of Missouri tax liability on the interest subsequently paid – interest that may, ultimately, be the result of the Illinois bank lending funds for

use in Missouri. The Court should rely on *Acme Royalty* to modify the *Union Electric* rule so as to bar corporations from protecting income from taxation through such a dodge.

II. Though corporations are required to pay tax on all income derived from Missouri, they may choose to use a statutory apportionment formula to calculate what portion of their total income is taxable, rather than accounting precisely for each dollar.

Ultimately, however, the question here need not be whether the interest is itself Missouri source income. For although Missouri law permits corporations to allocate each dollar according to its actual source, it permits them to use alternative, simpler methods of determining how much of their income will be subject to Missouri tax – methods that merely approximate reality, but that save considerably on bookkeeping and related expenses. These methods are called "apportionment." Properly applied, the apportionment method chosen by Medicine Shoppe includes the investment income in the formula.

Missouri law provides for two alternative "apportionment" formulas – and addresses when a corporation can and should instead use the factually more complex precise accounting method. *See*

Maxland Development Corp. v. Director of Revenue, 960 S.W.2d 503, 505 (Mo. banc 1998). The two formulas are "single factor" apportionment, set out in § 143.451, and "three-factor" apportionment, set out in the Multistate Tax Compact, § 32.300, art. IV. Section 143.461 requires a corporation to elect single factor apportionment under § 143.451, unless the corporation is willing and able to "keep its books and records in such a manner as to show the income applicable to this state, including gross income and deductions applicable thereto." The Compact, though not referenced as an alternative in § 143.461, applies to "[a]ny taxpayer subject to an income tax whose income is subject to apportionment and allocation for tax purposes." § 32.200, art. III § 1. That would include, of course, companies such as Medicine Shoppe that can apportion under § 143.451.

Subsections 143.451.1 and 143.451.2 each contain the rule that all income even partially derived from Missouri sources is taxed. Subsection 2 then authorizes the taxpayer to use the "single factor apportionment" formula to compute the portion of its entire income that will be deemed to have been derived from Missouri sources – *i.e.*, "to compute the portion of income from all sources in this state." § 143.451.2(2).

That, like three-factor apportionment under the Compact, is nothing more than an alternative to precise accounting – to "keep[ing] books and records in such manner as to show the income applicable in this state, including gross income and deductions applicable thereto" (§ 143.461.1). It is necessarily an imprecise instrument. It always saves the taxpayer bookkeeping costs. But sometimes it will result in a calculation that overstates the amount of income that would be attributable to Missouri under precise accounting; other times it understates that income. Three-factor apportionment has a similar impact. Presumably taxpayers choose their method of accounting and apportionment according to which one will result in the lowest net cost, taking into account both taxes owed and accounting expenses incurred.

III. "Single factor" apportionment calculates Missouri taxable income by applying a ratio to a taxpayer's "net income" – which includes non-Missouri income.

For the tax years in question, Medicine Shoppe chose "single factor apportionment" under § 143.451. The formula is set out in § 143.451.2(2).

That subsection begins in (a) with another broad statement – never construed by this Court: "The income from all sources shall be determined as provided." § 143.451.2(2)(a). The statute then states an exception – the sole exception to the "all income" rule: "income" does not include "the figures for the operation of any bridge connecting this state with another state." *Id*. Obviously that archaic exception does not apply here.

The next portion of the subsection, instead of making any additional exceptions, sets out the "single factor" formula. That formula is based on four figures, though there are two choices for the first three figures.

Many taxpayers use three sales figures: (1) "[t]he amount of sales which are transactions wholly in this state," "the amount of sales which are transactions partly within this state and partly without this state," and "total sales." § 143.451.2(2)(b). But for some, sales figures aren't a good measure of corporate activity. Thus, "where sales do not express the volume of business," the same calculation can be based on "business transacted" instead of "sales . . . transactions." *Id*.

The three "sales" or "business" figures are then used to calculate a ratio:

The amount of sales which are transactions wholly in this state shall be added to one-half of the amount of sales which are transactions partly within this state and partly without this state, and the amount thus obtained shall be divided by the total sales . . . .

Id. The calculation may be expressed in this formula:

$$\frac{\text{In-state sales} + \tfrac{1}{2}\text{ (Part-in-state sales)}}{\text{Total sales}}$$

Again, the result is a ratio showing the relationship between business done in Missouri and "total sales" or "total amount of business conducted."

That ratio is then applied to the fourth figure in the formula: "net income": "the net income shall be multiplied by the fraction thus obtained, to determine the proportion of income to be used to arrive at the amount of Missouri taxable income." *Id*. The entire formula, then, may be expressed as:

$$\frac{\text{In-state sales} + \tfrac{1}{2}\text{ (Part-in-state sales)}}{\text{Total sales}} \times \text{Net income}$$

"Wholly within this state," "partly within this state," and the converse of each is defined by statute, though only for "transaction[s] involving the sale of tangible property." § 143.451.2(3)(a), (b), and (c). By contrast, the key term here, "net income," is not defined in the statute. But it is a familiar term. As defined in Black's Law Dictionary (7th Ed. 1999) at 767, "net income" is "[t]otal income from all courses minus deductions, exemptions, and other tax reductions." That is consistent with the more general dictionary definition of "net": "free from all charges or deductions, as . . . remaining after the

deductions of all charges, outlay, or loss <~earnings> <~proceeds> – opposed to *gross*." Webster's Third New International Dictionary (1993) at 1519. And it is consistent with the use of "net income" elsewhere in Missouri statutes. For example, with regard to taxation of banks, "'Net income' means gross income . . . minus the deductions allowed." §§ 148.040.2, 148.150.1. When the code refers to something less than total income, it makes the distinction clear. *E.g.*, § 148.381.1 ("federal distributable net income"). Here, "net income" refers to "income from all sources" (§ 143.451.2(2)), not just from some.

Section 143.461.1 reiterates that inclusive reading. That section requires each corporation that elects single-factor apportionment "to determine income applicable to this state by multiplying the total income from all sources by the fraction determined in the manner set forth in section 143.451." The "fraction" spoken of is the "ratio" described above. "Income from all sources" is used in lieu of "net income." In other words, again, "net income" in § 143.451.2(2)(b) must mean "net income from all sources"; otherwise, § 143.461 would conflict with § 143.451.

The logic of reading the statute to apply the fraction or ratio to income from all sources is apparent from its application in a series of hypotheticals.

The first is the simplest. Assume that Corporation A has $1500 in total sales, $750 wholly within Missouri and $750 wholly outside Missouri. If the corporation were to use single-factor apportionment, the formula would work like this:

$$\frac{\$750 + \frac{1}{2}(0)}{\$1500} \times \$1500 = \$750$$

So $750 would be taxable – precisely the same figure that the corporation would reach if it did not choose an apportionment formula.

The second brings the complication of sales "partly within this state and partly without this state" – the complication that justifies the existence of apportionment formulas. Here, Corporation B has $1500 in total sales, $500 each in the wholly within, part within, and wholly without the state categories. The formula would work this way:

$$\frac{\$500 + \frac{1}{2}(\$500)}{\$1500} \times \$1500 = \frac{1}{2}(\$1500) = \$750$$

Again, this approach excuses Corporation B of having to somehow determine which dollar from the part-in-state sales is "derived from Missouri." The resulting $750 would overstate the actual Missouri-

derived sales (to Corporation B's advantage) if the majority of the $500 involved little Missouri activity. Or it would understate actual Missouri-derived sales (to the detriment of the State) if the majority of the $500 involved considerable Missouri activity. But Missouri has chosen to give corporations the choice.

And having made that choice, Medicine Shoppe should be required to calculate its taxable income as the words of the statute require.[1]

IV. The Court should overrule *Brown Group* to the extent it departs from the statutory scheme by exempting some income from the formula.

Imposing that requirement on Medicine Shoppe would require, unfortunately, that this Court reverse an incorrect precedent: *Brown Group, Inc. v. Administrative Hearing Commission*, 649 S.W. 2d 874 (Mo banc 1983).

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[1] This application of the statute is consistent with the one used for a passive investment, "triple net lease," in *Maxland Development Corp. v. Director of Revenue*, 960 S.W.2d at 506-07. There, the income from the lease, though "non-Missouri income," was included in the single-factor formula.

In *Brown Group*, the taxpayer asked the Court to exclude "royalties from a corporation of a foreign nation [from] the multiplicand," *i.e.*, from "net income" as that term is used in "the single factor formula." *Id*. at 879. The Director argued – as she does here – that "when a taxpayer elects under § 143.451.2(2) to apportion income using the single factor formula it is precluded from allocating any of its income prior to apportionment." *Id*. The Court rejected the Director's view. The Court's analysis began with a true statement: that § 143.451.1 "restrict[s] taxation of a corporation's income to that derived from sources within this state." *Id*. at 879-880. But from that point forward, the Court erred.

Subsection 2 does not establish a rate for taxing "income derived from sources within this state." § 143.451.1. It does not even define "income derived from sources within this state." As discussed above, it merely establishes an optional method for calculating taxable income without ever having to decide, dollar by dollar, which were "derived from sources within this state."

In some cases, the *Brown Group* rule makes no difference. That is evident from applying it to the first hypothetical set out above. Again, assume that Corporation A has $1500 in total sales, $750 wholly within Missouri and $750 wholly outside Missouri. If the

corporation were to use single-factor apportionment as set out in *Brown Group*, the formula would work like this:

$$\frac{\$750 + \frac{1}{2}(0)}{\$1500} \times \$1500 = \$750$$

So $750 would be taxable – the same as under the Director's reading of the statute. The same is true in the second hypothetical. Again, Corporation B has $1500 in total sales, $500 each in the wholly within, part within, and wholly without the state categories. The *Brown Group* formula would work this way:

$$\frac{\$500 + \frac{1}{2}(\$500)}{\$1000} \times \$1000 = 3/4\ (\$1000) = \$750$$

So both Corporations A and B end up with the same taxable income, regardless of whether *Brown Group* is used. In each instance, the tax may be more or less than what the company would owe with precise accounting, or with three-factor apportionment.

The differences arise when the variables are changed in two ways: to remove "passive" investment income, and to include expenses.

The impact of investment income is shown by two hypotheticals. Corporations C and D each have $2000 in income, all from Missouri, $1000 each from sales and interest earned on a bank deposit. Corporation C makes its deposit in a bank in Missouri.

Under either the Director's reading or *Brown Group*, it would apply the formula like this:

$$\frac{\$2000 + \frac{1}{2}(\$0)}{\$2000} \times \$2000 = 1x\ (\$2000) = \$2000$$

Corporation D makes its deposit in another state. Under the Director's reading, the calculation for Corporation D would be precisely the same as for Corporation C. But under *Brown Group*, Corporation D would obtain a very different result:

$$\frac{\$1000 + \frac{1}{2}(\$0)}{\$1000} \times \$1000 = 1x\ (\$1000) = \$1000$$

Corporation D reduces its taxable income by half merely by making its bank deposit across the state line. Nothing in the language or history of the Missouri statute suggests the legislature ever intended to encourage companies to invest *outside* the state. Yet that is precisely what the reading in *Brown Group* (like the *Union Electric* rule, discussed in I) accomplishes.

Expenses also result in an unacceptable difference under *Brown Group*. Passive investments often carry few expenses. When a corporation's expenses are allocated to sales or other business, and passive investment income is removed from the formula, *Brown Group* results in a skewed picture of real corporate income. Again we have two – necessarily much more complex – hypotheticals.

Corporation E, with total income of $1,500, has regular sales of $1,000 ($500 in Missouri; $500 partly in Missouri) and out-of-state investment income of $500. It has expenses (deductions) of $800, all related to the regular sales. On its federal return, it states $1,500 income less $800 deductions = $700 net income. Assuming no Missouri modifications or other deductions, Corporation E's tax is computed as follows:

	Per Director	Per *Brown Group*
Fed taxable income	700	700
Modifications	-0-	-0-
MO taxable inc-all sources	700	700
App factor = 0.750	$\frac{500 + ½ (500)}{1500} = 0.500$	$\frac{500 + ½ (500)}{1000}$
MO taxable inc-all sources	700	700
Less non-MO source inc	-0-	500
Apportionable income	700	200
Apportioned income	350	150
MO income percentage 0.214	350/700 = 0.500	150/700 =
MO taxable income	350	150

Brown Group keeps income out of the formula, thus dramatically reducing Missouri taxable income.

That contrasts with the case where expenses are level across all types of income. Corporation F is like Corporation E, but with expenses the same for all income ($533 expenses on the sales, $267 expenses on investments):

	Per Director	Per *Brown Group*
Fed taxable income	700	700
Modifications	-0-	-0-
MO taxable inc-all sources	700	700
App factor = 0.750	500 + ½ (500) / 1501 = 0.500	500 + ½ (500) / 1000
MO taxable inc-all sources	700	700
Less non-MO source inc	-0-	233 (500 – 267 expenses)
Apportionable income	700	467
Apportioned income	350	350
MO income percentage 0.500	350/700 = 0.500	350/700 =
MO taxable income	350	350

The contrast with Corporation E demonstrates the impact of *Brown Group* when a corporation has passive investment income (again, the kind of income that should be taxable in Missouri under *Acme Royalty*).

The problematic *Brown Group* reading is not required by § 143.451.1.

Rather, it is barred by that subsection, for the reading effectively exempts from taxation income at least some income derived from Missouri – despite the absence of any indication anywhere in Chapter

143 that the legislature intended such an exemption, and despite the presence of an explicit, inapplicable exemption in § 143.451.2(2)(a). In essence, the *Brown Group* rule says that § 143.451 creates a ratio that approximates what portion of a corporation's total income is actually derived from Missouri, then multiples only Missouri-derived income by that ratio to effectively remove from taxation a portion of that income. The Court should reverse its holding in *Brown Group* and reinstate the law as written.

The Court should not decline to take that step on the premise of legislative acquiescence, for a simple reason: the statute is already clear on its face – not just in § 143.451, but in § 143.461.1. Any additional language in a effort to legislatively reverse *Brown Group* would needlessly complicate the pertinent provisions.

Nor should the Court rely, as it did in *Brown Group*, on the rule that "tax statutes are to be strictly construed in favor of the taxpayer and against the taxing authority" (649 S.W. 2d at 881). Again, the language of the statute is unambiguous; there is no room for construction. And the option of using an apportionment formula to reduce taxable income should be treated, for construction purposes, as an exemption or a deduction. By giving taxpayers the option among three methods of calculating Missouri income, the legislature

was acting as it does when granting exemptions or deductions: it was removing from taxation some income that otherwise would be taxed. To recognize that the General Assembly let taxpayers choose a method of calculating Missouri taxable income according to which one reduces their tax liability – *i.e.*, which one costs the state the most – and at the same demand that each option be read to further benefit the taxpayer, is to go beyond what any reasonable reading of legislative intent could justify.

CONCLUSION

For the reasons stated above, the decision of the Administrative Hearing Commission should be reversed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that two copies of the foregoing

were mailed, postage prepaid, via United States mail, on this 17th day of

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CERTIFICATION OF COMPLIANCE

The undersigned hereby certifies that the foregoing brief complies with the limitations contained in Rule 84.06, and that the brief contains 5,314 words.

The undersigned further certifies that the disk simultaneously filed with the hard copies of the brief has been scanned for viruses and is virus-free.

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James R. Layton